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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 1021.

LEGH R. POWELL, JR. and HENRY W. ANDERSON, as Receivers of the Properties of Seaboard Air Line Railway Company,

Petitioners,

against

MARYLAND TRUST COMPANY, as Successor Trustee under the First Mortgage of Seaboard Air Line Railway dated April 14, 1900.

Respondent.

PETITION AND SUPPORTING BRIEF FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

W. R. C. COCKE,
HAROLD J. GALLAGHER,
GEO. V. CREDLE, JR.,
Attorneys for Petitioners,
Receivers of Seaboard Air
Line Railway Company.

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against

MARYLAND TRUST COMPANY, as Successor Trustee under the First Mortgage of Seaboard Air Line Railway dated April 14, 1900.

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

To the Honorable the Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

Legh R. Powell, Jr. and Henry W. Anderson, as Receivers of the properties of Seaboard Air Line Railway Company, pray that a writ of certiorari issue to review the decree of the United States Circuit Court of Appeals for the Fourth Circuit, entered in the above

case on January 6, 1942 (R. 199),* modifying and affirming the decree of the District Court of the United States for the Eastern District of Virginia (R. 192).

JURISDICTION.

The decree of the Circuit Court of Appeals sought to be reviewed was entered on January 6, 1942. The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended by the Act of February 13, 1925 [C. 229, 43 Stat.; 28 U. S. C., Sec. 347(a).]

STATEMENT.

On or about September 28, 1901 Seaboard Air Line Railway, predecessor of Seaboard Air Line Railway Company, delivered to The Continental Trust Company, as Trustee under its First Mortgage, (Maryland Trust Company being now the successor Trustee), certificates for 4,450 shares of the capital stock of Richmond-Washington Company, a holding company controlled by stock ownership in equal proportions by the Seaboard and five other railroads. These shares were purchased with funds obtained by the Railway Company from the sale of Refunding Collateral Trust Bonds pursuant to a Trust Agreement, dated May 1, 1901, between the Railway Company and Central Trust Company of New York, as Trustee, and in accordance with that agreement the shares were delivered to The Continental Trust Company to be subjected

* The typewritten transcript of the entire record is on file with the Clerk of this Court. The parties have stipulated that for purposes of this petition only the joint appendix to the briefs of the parties in the court below and the proceedings below need be printed.

by pledge to the lien of the First Mortgage. The pertinent pledge provisions of this Mortgage are shown on pages 28 et seq. of the record,—and are quoted in the brief annexed hereto in support of this petition.

On October 31, 1930, the authorized capital stock of the Richmond-Washington Company was $3,000,000, divided into 30,000 shares having a par value of $100 per share. On that date there were issued and outstanding 26,700 shares of its capital stock, of which Seaboard Air Line Railway Company owned 4,450 shares, the same shares above referred to as pledged under the First Mortgage. The issued capital stock of the Richmond-Washington Company was increased on October 31, 1930, by the payment of a fifty per cent stock dividend, the payment of which had previously been approved by the directors and stockholders of the Company at duly called meetings. This dividend represented surplus derived wholly from profits and earnings of the Company. Immediately before the issuance of the stock dividend the book value of each of the original shares was $263.75, and immediately thereafter the book value of each of the old and the new shares was $175.83. As the 4,450 shares owned by the Railway Company, and held by the First Mortgage Trustee, were registered in the name of the Railway Company, the Railway Company prior to the Receivership received delivery of the fifty per cent stock dividend consisting of 2,225 shares. Upon receipt thereof the Railway Company continued to hold the certificates for the 2,225 shares, and upon the appointment of the Receivers of the Railway Company on December 23, 1930, the Receivers continued and still continue to hold the certificates for such shares in their possession.

Between their appointment on December 23, 1930 and December 30, 1931, inclusive, the Receivers were paid $53,400.00 in cash dividends upon the 4,450 shares pledged with the First Mortgage Trustee. In addition, the Receivers have received cash dividends of $114,031.25 from December 31, 1930 to date upon the stock dividend of 2,225 shares in the possession of the Receivers. These amounts include a cash dividend of $20,025.00 declared and payable to stockholders of record as of December 18, 1930, but not paid until December 31, 1930. Further dividends after 1931 on the 4,450 shares have been paid to the First Mortgage Trustee by the Richmond-Washington Company on demand of the Trustee,—the Receivers having conceded the validity of the pledge of the 4,450 shares and the right to the cash dividends thereon declared after demand by the Trustee that further dividends on the 4,450 shares be paid to it.

The Trustee of the First Mortgage made no claim whatever of a right to possession of the 2,225 shares until April 15, 1938, when a joint written demand by the Trustee of the First Mortgage and the Trustees of the Seaboard Air Line Railway Refunding Mortgage, who also claim a right to the 2,225 shares under the provisions of that mortgage, was served on the Receivers for delivery of the shares and payment over to the Trustee of the First Mortgage of the amounts of the dividends paid to the Receivers on both the 4,450 shares and on the 2,225 shares. The amounts of the dividends then aggregated $142,956.25, including $20,025.00 payable on December 31, 1930, to stockholders of record of the Richmond-Washington Company as of December 18, 1930.

On April 10, 1931, at a hearing upon the Receivers' application for authority to issue and presently sell $4,000,000 of Receivers' Certificates, there was introduced by the Receivers a statement of unpledged securities owned by Seaboard Air Line Railway Company as of December 23, 1930. This statement lists stocks of Richmond-Washington Company at a par value and book value of $222,500.00, and shows this stock as being 16⅔% of the stock of the Richmond-Washington Company owned by the Railway Company. This, of course, referred to the 2,225 stock dividend shares. The hearing on this application resulted in a decree, dated April 22, 1931, providing for a lien in favor of the Receivers' Certificates

> "(1) upon the surplus earnings and income hereafter coming into the hands of the Receivers, after paying out of such earnings and income, however derived, the expenses of the receivership and of operation, and such other amounts for similar purposes as the Court may direct, and upon any property or interest therein purchased with such surplus earnings and income; and
>
> "(2) upon all the property and assets of every nature and description of the Railway Company and/or the Receivers, whether real, personal or mixed, now or at any time hereafter in the possession or under the control of the Receivers (including, without limitation of the foregoing general description, securities, evidences of indebtedness, rolling stock, other equipment, and the interest of the Railway Company and/or the Receivers in equipment under equipment agreements).

prior to any lien thereon, direct or indirect, of the following general mortgages of the Railway Company, viz.:

> "First Mortgage, dated April 14, 1900, to The Continental Trust Company, Baltimore, Maryland, Trustee, and all supplements thereto;
>
> "Refunding Mortgage, dated October 1, 1909, to The New York Trust Company and Mortimer N. Buckner, as Trustees; * * *" (R. 125).

Thereafter, when the Receivers' Certificates issued under this decree were refunded pursuant to the provisions of a decree entered on February 15, 1933, which also authorized a large amount of additional certificates, and when the Receivers' Certificates issued under this latter decree were again refunded by decrees entered on March 20, 1935, authorizing the issuance of an aggregate of more than $23,000,000 of certificates, the identical provisions as to lien were embodied in these decrees and the statement showing unpledged securities was introduced and made a part of the record on the hearings preceding each of these later decrees. At all of these hearings the Trustee of the First Mortgage and the Trustees of the Refunding Mortgage were parties to the proceedings and were represented at the hearings by counsel, but asserted no rights to the 2,225 shares.

As the Receivers took the position that neither the Trustee of the First Mortgage, pursuant to the pledge provisions of the First Mortgage above referred to (R. 46), nor the Trustees of the Refunding Mortgage, were entitled to the possession of the 2,225 stock dividend shares or the cash dividends declared

thereon, and were not entitled to the pledge of cash dividends declared on the 4,450 shares pledged with the Trustee until demand was made therefor by the Trustee, and that the appointment of the Receivers constituted an equitable lien in favor of other creditors upon the stock and cash dividends collected by the Railway Company, and that the decrees of the District Court authorizing the issuance of Receivers' Certificates subjected to the lien of the certificates the stock and cash dividends collected by the Railway Company, the joint written demand by the Trustee of the First Mortgage and the Trustees of the Refunding Mortgage was refused.

Thereafter, on November 23, 1938, the Trustee of the First Mortgage and the Trustees of the Refunding Mortgage simultaneously filed petitions in the Consolidated Receivership Cause of Seaboard Air Line Railway, pending in the District Court of the United States for the Eastern District of Virginia, seeking possession and control of the stock and cash dividends collected by the Railway Company and by the Receivers after their appointment on December 23, 1930.

The controversy was referred by the District Court to a Special Master, who, in a report filed June 19, 1940 (R. 132), found for the First Mortgage Trustee, both as to the stock dividend and the total of the cash dividends claimed. This report was affirmed on June 28, 1941, by the District Court, except as to the cash dividend of $20,025.00 paid December 31, 1930, which was held to belong to the Receivers (R. 192). The Special Master held that the 2,225 shares had not been subjected to the lien of the Receivers' Certificates, giving as the reason that the record on the proceedings

for the issuance of the certificates failed to show that the Trustee of the First Mortgage was aware of an intention to subject the shares to the lien of the certificates and though represented in all the proceedings by counsel was not concluded by the language of the decrees, or by the evidence introduced by the Receivers showing that they claimed the 2,225 shares as a free asset of the Receivership Estate, which were to be subjected to the lien of the certificates. In confirming the Master's report the District Court paid no attention to the point (Memorandum Opinion, R. 185). The majority opinion of the Circuit Court of Appeals seems to have accepted the reasons given by the Master, but attaches little importance to the question. All parties appealed from the decree of the District Court, and on January 6, 1942, the court below, Soper, Circuit Judge, dissenting, affirmed this decree as modified by the adding of the amount of the dividend of December 31, 1930, $20,025.00, to the amount of the dividends which the Receivers were ordered to pay over and deliver to the First Mortgage Trustee (R. 169).

QUESTIONS PRESENTED.

1. The case involves the proper interpretation of a clause in the Seaboard Air Line Railway First Mortgage relating to the rights as between the railroad pledgor and the mortgage trustee as pledgee. It also involves questions as to the rights of the Trustees of Seaboard Air Line Railway Refunding Mortgage, who were appellants also in the court below. The parties, the District Court and the Circuit Court of Appeals all agree that the law to be applied in interpreting the pledge provisions of the First Mortgage is the law of

Maryland, which is the *forum contractus*, but Petitioner contends that neither the District Court nor the Circuit Court of Appeals applied the law of the State but on the contrary, ignored it and exercised an independent judgment as to what the law is, instead of following the decisions of the highest Court of the State.

2. Another question having an important bearing upon values of property and securities that must be considered in a reorganization of the Seaboard Air Line Railway is whether or not, irrespective of the question of interpretation of the mortgage, any inchoate rights of the trustees of the mortgages involved were subordinated to a paramount lien in favor of Receivers' Certificates issued pursuant to decrees of the Courts of jurisdiction of the Seaboard Air Line Railway Receivership and found to be necessary for the proper maintenance and operation of the railway properties in the interest of the public and of the security holders of the railway.

STATUTE INVOLVED.

Section 34 of the Federal Judiciary Act of September 24, 1789 (1 Stat. at L. 92), chap. 20, 28 U. S. C. A., Sec. 725, provides as follows:

> "The laws of the several States, except where the Constitution, treaties, or statutes of the United States otherwise require or provide, shall be regarded as rules of decision in trials at common law, in the courts of the United States, in cases where they apply."

SPECIFIC ASSIGNMENTS OF ERROR TO BE URGED.

The court below erred:

1. In holding the Trustee of the First Mortgage to be entitled to a lien upon and the possession of the 2,225 shares of Richmond-Washington Company declared as a stock dividend upon the 4,450 shares of the stock of said Company owned by Seaboard Air Line Railway Company and held in pledge by the Trustee under the First Mortgage.

2. In holding the Trustee of the First Mortgage to be entitled to a lien upon and the possession of $53,400.00, representing cash dividends paid from December 31, 1930 to December 31, 1931 upon the 4,450 shares of stock held by the Trustee in pledge under the First Mortgage, and $114,031.25, representing cash dividends paid the Receivers from December 31, 1930 to date by Richmond-Washington Company upon the 2,225 stock dividend shares held by the Receivers.

3. In holding that the lien of the First Mortgage was not subordinated to the liens of the Receivers' Certificates under the decrees of the Courts administering the Receivership.

REASONS FOR GRANTING THE WRIT.

This case comes within the provisions of Paragraph 5(b) of Rule 38 of this Court.

1. The Circuit Court of Appeals for the Fourth Circuit has here erroneously failed to apply the ap-

plicable Maryland law with respect to the nature of a stock dividend upon shares of capital stock of a corporation, a question of public importance concerning the interrelation of State and Federal Courts, and has rendered a decision in conflict with the decisions of this Court.

This Court in the cases of *Erie R. Co.* v. *Tompkins*, 304 U. S. 64, 82 L. Ed. 1188; *Ruhlin* v. *New York L. Ins. Co.*, 304 U. S. 202, 82 L. Ed. 1290; *West* v. *American Teleph. & Teleg. Co.*, 311 U. S. 223, 85 L. Ed. 139, and others, has declared that except in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State.

Although the Maryland common law with respect to the nature of a stock dividend was firmly established by a long line of decisions of the Court of Appeals of Maryland, beginning with *Thomas* v. *Gregg*, 78 Md. 545, 28 Atl. 565, and summed up in *Heyn* v. *Fidelity Trust Co.*, 174 Md. 639, 1 Atl. (2d) 83, when the pledge under consideration in this case was made, the majority of the court below concluded that it was free to exercise an independent judgment as to what the law is, and arrived at its conclusion by resort to contrary decisions of the courts of Missouri, Virginia, North Carolina and the United States.

2. The Circuit Court of Appeals, as did the District Court, ignored the decrees directing the issuance of the Receivers' Certificates and providing for a lien security for such certificates, upon which decrees the holders of such certificates, for whom the Receivers are in a sense trustees, had a right to rely and in view of

the record in those proceedings assume that the lien of the certificates covered the 2,225 shares of stock. The facts in greater detail are shown in the brief annexed hereto in support of this petition.

Wherefore, it is respectfully submitted that this petition for a writ of certiorari should be granted.

March 5, 1942.

W. R. C. Cocke,
Harold J. Gallagher,
Geo. V. Credle, Jr.,
For Petitioners.